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Congress of the United States

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Washington, DC 20515–2404

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QA - 279956

May 3, 2004

Docket Management Facility
U.S. Department of Transportation
400 Seventh Street SW, Room PL-401
Washington, DC 20590-0001

RE: Comments to Commandant Thomas H. Collins
Coast Guard Docket No. USCG-2003-14472 – 35

Dear Admiral Collins:

The Jones Act is a critical component of our nation's military and economic security, and the U.S.-citizen ownership and control requirements are a foundation of that law. In enacting the vessel lease finance provisions, the United States Congress did not intend to undermine the Jones Act. Misapplication of the vessel lease finance provisions has significant competitive consequences for the domestic maritime industry. Companies establishing elaborate schemes to circumvent the intent of the law have used transfer pricing and tax advantages to compete unfairly in the domestic trades and to undermine the Jones Act, harming U.S. shipyards, labor, and other operators. As a Member of the House Transportation & Infrastructure Committee and the House Armed Services Committee, I can assure you that this was never the intent of Congress.

The Coast Guard's final rule on lease financing as published on February 4, 2004, made significant progress toward implementing regulations to govern permissible lease financing arrangements. The agency rightly considered the intent and spirit of the Jones Act in developing its rule. By doing so, the Coast Guard has taken commendable steps to partially close the Jones Act loopholes that have been exploited by some foreign shipping companies using lease financing. The additional joint agency rulemaking now proposed by the Coast Guard and the Maritime Administration offers an opportunity to effectively complete the job of closing such loopholes.

By prohibiting a vessel lease financing owner from chartering a lease financed vessel back to itself or an affiliate, foreign shipping companies will no longer be able to use lease financing to compete unfairly against bona fide domestic Jones Act operators. Therefore, the proposed §67.20(a)(9) should be adopted. The joint rule should prohibit all charters and sub-charters of a lease financed vessel back to the vessel's owner, except in the case of a lease financed vessel used to carry proprietary cargo. To be most effective, charter back arrangements should be prohibited where they govern not only the vessel's operations, but also its business use if not for proprietary operations. This prohibition will help to ensure that foreign tax advantages relevant to the business use of

vessels do not place domestic companies offering for-hire maritime services to third parties at a competitive disadvantage. By contrast, the alternatively proposed §67.20(a)(6) should not be adopted. By the Coast Guard's own admission, this provision is incomplete and would leave many questions unresolved regarding the chartering back of a lease financed vessel. We must prevent rather than facilitate any further muddying of the quagmire waters.

It is crucial to acknowledge a distinction between the business use of a vessel and its mechanical operations in the context of vessel lease financing arrangements. No matter how cleverly convoluted the organizational structure of a lease financing transaction may be in its efforts to give the appearance of adhering to the letter of the law, the primary Jones Act issue is *control*. The immediate physical control of a lease financed vessel is incidental, however, to the overall control of its purpose as a pawn in the grand scheme of the arrangement. Operational control of a vessel, then, should not be confused with control of operations in the larger sense.

If an economically superior foreign entity ultimately pulls the strings that control the behavior of their domestic affiliate, then the intent of the Jones Act has been thwarted. At that point, the domestic affiliate is economically dependent upon the foreign entity to the extent that the arrangement serves as a siphon, drawing the profits from our coastwise trades effortlessly across an ocean. Vessel lease financing is intended by Congress to facilitate passive investments by bona fide financial institutions. Vessel lease financing is not intended by Congress to facilitate indirect economic control over domestic operators by foreign entities seeking clandestine entry into the Jones Act trades.

The underlying motivation for devising multi-layered, international schemes is precisely the type of thing the Jones Act has outlawed. That motivation for foreign shipping companies is to obtain a foothold from which to funnel themselves the lion's share of commercial profits from the American coastwise trades while avoiding paying U.S. taxes. If successfully manifested, its effect will increasingly and ultimately be to eliminate American jobs, presenting a very real threat to our industrial base. The Jones Act exists to protect the United States from this type of parasitic relationship with foreign entities. If we effectively submit the economic control of our domestic trades to foreign entities, our national and economic security is compromised along with our law. As such, ensuring the integrity of the Jones Act is a matter of survival.

By all means, the joint agency proposed rulemaking should adopt maximum limitations on the grandfather provisions published in the final rule. As expressed in my comments of October 7, 2002 on the final rule, deletion of the grandfather provisions altogether would best ensure the preservation and integrity of the Jones Act. We are trying to stop the bleeding here, and a tourniquet is more effective than a bandage in that regard. Time is of the essence for many of the smaller Jones Act operators, who will not be able to survive three years' worth of head-on competition against operations that are financed and ultimately controlled by mammoth foreign conglomerates. The proposed three-year limitation on the grandfather provision will buy foreign organizations enough time to engage in anti-competitive behavior, which could dramatically reduce the size

and value of our domestic fleet. A bandage is better than nothing, but grandfathering will still result in negative consequences for the Jones Act.

Regarding third party audits of endorsement applications, the Coast Guard and the Maritime Administration should use all available powers to closely monitor them in enforcing the vessel lease finance rule. This is ultimately and inherently a governmental function and responsibility, however. Inadequate scrutiny on the part of the Coast Guard has contributed significantly to the problems associated with the application of vessel lease financing. It is critically important to fully review proposed vessel lease finance transactions, their commercial structure, and their implications - all *prior* to making determinations. As the Coast Guard, the Maritime Administration, and the industry have seen, addressing concerns after transactions are approved is fraught with difficulty. Transactions involving foreign shipping companies or charter back arrangements should especially raise a red flag of questionability. The Coast Guard should grant interested parties an opportunity to review and comment publicly on any questionable transactions *prior* to the issuance of documents.

Lastly, in determining the aggregate revenues test qualifications of a foreign entity, the Coast Guard should closely review prospective transactions that would result in the entity becoming non-compliant at some point in the future due to contractual arrangements. For example, the Coast Guard should not issue certificates to vessels where there is an indication that agreements or contractual relations exist that would cause the entity to fail the aggregate revenues test upon their consummation. Such careful scrutiny is necessary to prevent foreign conglomerates from utilizing lease financing to get a foot in the coastwise trades door that will facilitate their long-range intent to become primarily involved in shipping. These types of transactions should also raise a red flag of questionability, impropriety, and bad intent toward the Jones Act. As the Coast Guard well knows regarding lease finance transactions, enforcement of the letter, intent, and spirit of the Jones Act is paramount.

Sincerely,

GENE TAYLOR
Member of Congress